

No. 7884

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**In the United States Circuit Court of  
Appeals for the Ninth Circuit**

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**LOUIS M. GRAFE, PETITIONER**

*v.*

**COMMISSIONER OF INTERNAL REVENUE, RESPONDENT**

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**ON PETITION FOR REVIEW OF DECISION OF THE UNITED  
STATES BOARD OF TAX APPEALS**

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**BRIEF FOR THE RESPONDENT**

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**OPINION BELOW**

The only previous opinion in this case is the memorandum opinion of the Board of Tax Appeals (R. 12-17), which is unreported.

**JURISDICTION**

This review involves income taxes against the petitioner amounting to \$12,023.08 for the taxable year 1929 (R. 22). The decision of the Board was entered October 29, 1934 (R. 18). The present petition for review was filed January 25, 1934 (R. 27), pursuant to the provisions of Sections 1001-1003 of the Revenue Act of 1926, c. 27, 44 Stat. 9,

109-110, as amended by Section 603 of the Revenue Act of 1928, c. 852, 45 Stat. 791, 873, and Section 1101 of the Revenue Act of 1932, c. 209, 47 Stat. 169, 286, and as further amended by Section 519 of the Revenue Act of 1934, c. 277, 48 Stat. 680, 760.

#### QUESTIONS PRESENTED

1. Whether the sum of \$55,000 representing dividends paid on certain stock of the Paris American Pharmacal Company was income belonging to the petitioner.

2. Whether the sum of \$2,242.50 representing interest paid on bonds and reported as income belonging to the petitioner's wife was income taxable to the petitioner.

#### STATUTE INVOLVED

Revenue Act of 1928, c. 852, 45 Stat. 791:

##### SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

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## STATEMENT

## I

In 1928, the petitioner, then a resident of Iowa, was the sole stockholder and director of the Paris American Pharmacal Company, a corporation organized under the laws of that State and having a total outstanding capital stock of \$7,000 divided into 70 shares of \$100 par value each (R. 12, 13). The corporation was engaged in a mail order business (R. 12), and appears to have been extraordinarily prosperous in 1928 (R. 13).

On February 14, 1929, the company declared a dividend of 500 per cent, and on February 28, 1929, another dividend of 500 per cent (R. 13-14). Prior to the declaration of these dividends, however, namely, on January 17, 1929, the petitioner transferred 25 shares of the stock to his mother-in-law, Ivy R. Lewis, and 30 shares of the stock to his wife, Loy Ola Grafe (R. 14). The declaration of dividends thus resulted in two dividends in the amount of \$7,500 each for the petitioner, two in the amount of \$12,500 each for his mother-in-law, and two in the amount of \$15,000 each for his wife (R. 14). A substantial portion of his wife's dividends was credited on the company's books to his own account (R. 15).

The stock held by the petitioner's mother-in-law appears to have been transferred to her merely as security to indemnify her against any loss that she might sustain by reason of her guaranty of a \$3,400 advertising account of the company (R. 15).



In January 1930, the petitioner moved to California, and the business of the company was thereafter conducted in that State. On February 10, 1930, the shares held by the petitioner's wife and mother-in-law were cancelled and reissued to the petitioner. About that time, one share each was issued to George B. Blake and Edith Williams, who then became directors of the company<sup>1</sup> (R. 15).

The taxes involved are for the year 1929. The petitioner did not report as income for that year the dividends declared with respect to the stock ostensibly held by his wife and mother-in-law. The Commissioner, however, determined that the transfers of stock by the petitioner were not bona fide, and that the petitioner being the real owner of the stock was accountable for the dividends (aggregating \$55,000), declared with respect to the stock so transferred.

The only witnesses before the Board of Tax Appeals were the petitioner himself, his wife and mother-in-law (R. 29-45). They attempted to show that prior to the year 1928, the petitioner's wife had certain funds which might have been furnished to the petitioner for the purpose of assisting in the organization of the corporation, and that she was really the owner of the stock not held in his name when the dividends were declared. The

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<sup>1</sup> Further transfers were subsequently made in 1932, when stock was again issued to the petitioner's wife (R. 16).



Board, however, was unconvinced by this testimony, and found as a fact that the transfers of stock "were lacking in bona fides" (R. 17).

## II

The second item in controversy for the year 1929 relates to interest in the amount of \$2,242.50 received from certain bonds during that year. The bonds in question were purchased from funds of the corporation during the period December 19, 1928, through April 1929, and were taken in the name of petitioner's wife (R. 14-15). Here, too, the bona fides of the stock ownership and the taking of title to the bonds by the one really interested is the pivotal question. The Board's finding as to lack of bona fides with respect to the major issue of stock ownership disposed of this issue also.

### SUMMARY OF ARGUMENT

The question involved in this case is one of fact only, namely, the bona fides of the transfers of January 1929. The Board found as a fact that the transfers were not bona fide. Unless the record compels a different result that finding must stand.

The only witnesses in support of the petitioner, however, were the petitioner himself, his wife and mother-in-law. But the mere fact that the respondent offered in rebuttal witnesses and that the result reached by the Board was at variance with their testimony does not as a matter of law entitle the petitioner to a reversal.

## ARGUMENT

This case presents solely a question of fact, namely, the bona fides of the stock transfers in January 1929. The Board of Tax Appeals found that those transfers "were lacking in bona fides" (R. 17). It is that finding which the taxpayer seeks to overthrow. He relies upon the "uncontradicted testimony" offered on his behalf before the Board.

The only witnesses below were the taxpayer himself, his wife, and mother-in-law—all standing in a confidential relationship to each other and directly interested in the outcome of this litigation. The fact that their testimony was uncontradicted does not impart to it a sanctity that would render contrary to law any finding of fact not in harmony therewith.

The Commissioner's determination was, of course, prima facie correct, and the burden of proof was on the taxpayer to overcome that presumption. *Helvering v. Taylor*, 293 U. S. 507, 514; *New Colonial Co. v. Helvering*, 292 U. S. 435, 440; *Welch v. Helvering*, 290 U. S. 111; *Burnet v. Houston*, 283 U. S. 223; *Reinecke v. Spalding*, 280 U. S. 227, 232-233; *Botany Mills v. United States*, 278 U. S. 282; *Wickwire v. Reinecke*, 275 U. S. 101, 105.

The Board determined that the presumption of correctness had not been overcome and therefore found as a fact that the transfers were not bona fide. Cf. *Wishon-Watson Co. v. Commissioner*, 66

F. (2d) 52 (C. C. A. 9th); *Rasmusson v. Eddy's Steam Bakery*, 57 F. (2d) 27 (C. C. A. 9th), certiorari denied, 287 U. S. 601. That finding is conclusive upon appeal unless the record compels a contrary result. *Commissioner v. Burdette*, 69 F. (2d) 410, 411 (C. C. A. 9th); *Tumwater Lumber Mills Co. v. Commissioner*, 65 F. (2d) 675, 676 (C. C. A. 9th); *Pedder v. Commissioner*, 60 F. (2d) 866, 869 (C. C. A. 9th); *Phillips v. Commissioner*, 283 U. S. 589, 599-600. Cf. *Peerless Investment Co. v. Commissioner* (C. C. A. 9th), decided December 17, 1935; *Commissioner v. Eldridge* (C. C. A. 9th), decided November 4, 1935.

The mere fact that he has presented testimony to the contrary does not entitle him as a matter of law to a finding in accordance with that testimony. The Board may well have disbelieved that testimony. It may well have been unconvinced as to the veracity of the witnesses. Their general demeanor on the witness stand, their tone of voice and possible hesitancy in answering questions, and other factors not susceptible of reproduction in a record upon appeal, may well have influenced the Board in its finding.

We respectfully submit that the determination of the Board, being one of fact only, should as a matter of law be sustained. The only basis offered by the petitioner tending to establish a contrary result is that the testimony, if believed, would support a different finding. But upon appeal, the

question is not whether the testimony would support a different finding but whether upon the record a different finding is compelled.

In *Slayton v. Commissioner*, 76 F. (2d) 497 (C. C. A. 1st), certiorari denied, October 14, 1935, a similar situation was presented. In that case the taxpayer had disposed of certain securities through a broker to her son. The bona fides of that transaction was drawn into question and vigorous testimony was introduced in support of its genuineness. As in the present case, the Government presented no witnesses. The Board of Tax Appeals found that the transaction was not bona fide. The taxpayer attempted to upset that finding as contrary to the "undisputed testimony", but the Circuit Court of Appeals rejected that contention, saying (pp. 498-499):

It is urged, because the taxpayer in this case testified that, acting upon her husband's advice, she indorsed the certificate of stock in question, and authorized her husband to deliver it to some broker for sale at a price established by her husband, and that she did not know her son had bought it until her husband told her and asked her if she was willing to give her son the money to pay for it, which she did, and because her son corroborated this testimony, and the government presented no witness who disputed it, a finding that the sale was not bona fide was contrary to the "undisputed evidence" and without any evidence to support it, and was

therefore erroneous in law. *Oral testimony may be "undisputed", but may not from all the evidence in the case constitute "indisputable evidence."* (Italics supplied.)

Similarly in the present case, the Board's finding should be sustained even though the taxpayer himself, together with his wife and mother-in-law, testified that the transfers were bona fide and the respondent presented no witnesses to contradict that testimony.

#### CONCLUSION

The decision of the Board of Tax Appeals should be affirmed.

Respectfully submitted.

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JANUARY 1936.

